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No. 86-561

IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1986

GEORGE F. GRODE, Insurance Commissioner
of the Commonwealth of Pennsylvania,
Petitioner

v.

UNITED SERVICES AUTOMOBILE ASSOCIATION,
a Texas Reciprocal Interinsurance Exchange, and
USAA CASUALTY INSURANCE COMPANY,
USAA LIFE INSURANCE COMPANY, and
USAA ANNUITY AND LIFE INSURANCE COMPANY,
Texas Stock Insurance Companies,
Respondents

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

RESPONDENTS' BRIEF IN OPPOSITION

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STATEMENT OF QUESTIONS PRESENTED FOR REVIEW

1. Where no adequate opportunity to raise federal challenges in state judicial proceedings existed because the federal plaintiffs would suffer "devastating economic consequences" from state administrative proceedings before their federal claims could be heard on appeal, did the Court of Appeals properly decline to abstain under *Younger*?

2. Should this Court review the Court of Appeals' factual "findings" of the devastating economic harm which would be caused by a *Pullman* abstention, especially where an alternate ground for not abstaining under *Pullman* was also present?

LIST OF PARTIES AND RULE 28.1 LIST

The parties to the proceedings below were William J. Muir, III, Acting Insurance Commissioner of the Commonwealth of Pennsylvania, and the Respondents United Services Automobile Association, USAA Casualty Insurance Company, USAA Life Insurance Company, and USAA Annuity and Life Insurance Company.[1] The Petitioner before this Court is George F. Grode, the current Insurance Commissioner of the Commonwealth of Pennsylvania.

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1. The parent of Respondent USAA Casualty Insurance Company and Respondent USAA Life Insurance Company is Respondent United Services Automobile Association ("USAA"), a Texas Reciprocal Interinsurance Exchange. The parent company of the fourth Respondent, USAA Annuity and Life Insurance Company, is Respondent USAA Life Insurance Company. Respondent USAA Life Insurance Company has another subsidiary, USAA Life General Agency, Inc. Respondent USAA has the following subsidiaries in addition to the above-mentioned Respondents: USAA Consumer Services, Inc., USAA Special Services Company, USAA General Indemnity Company, USAA General Agency, Inc., USAA Limited, USAA Satellite Communications Company, USAA CAF Company, USAA Real Estate Company, USAA Investment Management Company and USAA Capital Corporation.

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v.

UNITED SERVICES AUTOMOBILE ASSOCIATION,
USAA CASUALTY INSURANCE COMPANY,
USAA LIFE INSURANCE COMPANY, AND
USAA ANNUITY AND LIFE INSURANCE COMPANY,

Respondents

RESPONDENTS' BRIEF IN OPPOSITION

Respondents United Services Automobile Association, USAA Casualty Insurance Company, USAA Life Insurance Company and USAA Annuity and Life Insurance Company respectfully request that this Court deny the petition for certiorari, seeking review of the Third Circuit's opinion in this case. The opinion is reported at 792 F.2d 356 (3d Cir. 1986).

STATUTES INVOLVED

Section 5(a) of the Home Owners' Loan Act of 1933, *as amended*, 12 U.S.C. §1464(a) provides:

> [T]he Board is authorized, under such rules and regulations as it may prescribe, to provide for the organization, incorporation, examination, operation, and regulation of associations to be known as Federal savings and loan associations, or Federal savings banks, and to issue charters therefor, giving primary consideration to the best practices of thrift institutions in the United States.

STATEMENT OF THE CASE

United Services Automobile Association and its co-respondents (hereafter "USAA") are Texas-domiciled insurers duly licensed to transact insurance business in all fifty states, including Pennsylvania. USAA's member-policyholders are present and former officers in the United States armed forces — Army, Navy, Air Force and Marines. USAA, which does insurance business throughout the nation, received over $35,000,000 in premiums from its 40,000 Pennsylvania policyholders in 1983 alone.

USAA through a subsidiary applied for and obtained a federal charter and all necessary approvals from both the Federal Home Loan Bank Board (the "Board") and the Federal Savings and Loan Insurance Corporation (the "FSLIC") to establish, own and operate a new federal savings bank to be known as the USAA Federal Savings Bank (the "Bank") in San Antonio, Texas. In that process, these federal agencies were fully informed of USAA's deep involvement in the insurance business. Both these agencies approved the ownership of the Bank within the USAA group of companies, and imposed certain operational limitations and conditions on USAA. (1A-10A.)[2] The federal charter was issued and the new federal bank commenced its operations December 31, 1983.

The Bank has no operations, accepts no deposits, and does no business in Pennsylvania. (Pet. App. 46a, 3a.)

Regulation of the ownership, incorporation and operation of banks in the federal savings and loan system lies within the exclusive control of Congress and its designated agencies, the Board and the FSLIC. *See Fidelity Federal Savings and Loan Association v. de la Cuesta,*

2. References marked as (____A) refer to page ____A in the attached Appendix of respondents. References to Petitoner's Appendix are, e.g., Pet. App. __a.

458 U.S. 141, 160 (1982); 12 U.S.C. §1464(e); 12 C.F.R. §§541 *et seq.*

In mid-1984, the Pennsylvania Insurance Department notified USAA that its ownership of the Bank, although approved by the two federal agencies, was prohibited by Section 641 of the Pennsylvania Insurance Department Act of 1921, as amended, 40 P.S. §281. Section 641(b) prohibits insurers licensed to do business in Pennsylvania from owning or being affiliated with any "lending institution, . . . bank holding company [or] savings and loan holding company." 40 P.S. §281(b). Petitioner's Insurance Department then advised USAA of its choices: it must either divest itself of its new federal savings bank (in which USAA had invested over $20,000,000), or face revocation of its Pennsylvania insurance licenses and attendant loss of its substantial (over $35,000,000 in annual premiums) Pennsylvania insurance business.

Faced with this conflict between its federally-approved bank ownership and the prohibitions of Pennsylvania law, USAA commenced this civil rights action in federal court under 42 U.S.C. § 1983. The suit, filed on November 27, 1984, sought declaratory and injunctive relief against Pennsylvania's Acting Insurance Commissioner (hereafter "Commissioner" or "petitioner"), the state official responsible to enforce Pennsylvania's insurance laws. No state proceeding of any sort was then pending.

The Complaint's Supremacy Clause challenge did not attack the facial validity of Section 641(b) but averred that the statute was unenforceable if and as applied to USAA's affiliation with the Bank, because the organization, ownership, and operation of that Bank (and its parent savings and loan holding company) are preempted from state regulation by the Home Owners' Loan Act of 1933, as amended, 12 U.S.C. §1461 *et seq.*, by the National Housing Act, as amended, 12 U.S.C.

§§1730, 1730a, the regulations implementing these statutes and by federal agency actions thereunder. The Complaint also raised several issues of pure constitutional interpretation under the Commerce, Equal Protection and Due Process Clauses of the United States Constitution.

On December 24, 1984, the Commissioner's Insurance Department commenced an administrative license revocation proceeding by issuance of a Show Cause Order, alleging that USAA was in violation of Section 641 and that revocation of all respondents' insurance licenses was required. (1A-16A.) Under applicable Pennsylvania procedure, the Commissioner himself will decide the outcome of this proceeding. On the same day, counsel for the Commissioner filed in the district court a Motion to Dismiss the federal Complaint on grounds of *Pullman* and *Burford* abstention only, urging that the pendency of the license revocation proceedings (commenced only that same day) warranted such abstention. The Commissioner's own internal documents, obtained in discovery, showed that the administrative proceedings were themselves instituted, as later noted by the Court of Appeals (Pet. App. 74a), to defeat federal jurisdiction.

On January 25, 1985, USAA filed in the District Court a Motion for Summary Judgment on Preemption Grounds. USAA also filed a Motion for Preliminary Injunction to enjoin the revocation proceedings and briefed both motions. These motion papers advised the district court of the devastating economic harm which a license revocation order would cause USAA in the marketplace. The district court never addressed these motions.

Instead, relying on the pendency of the Insurance Department's administrative proceedings and various abstention doctrines, including the *Younger* doctrine

(never argued or briefed), the district court on September 30, 1985 abstained and dismissed respondents' Complaint. The district court identified a single state interest to be served by abstention—the state's authority to regulate the insurance industry as manifested by the McCarran-Ferguson Act, 15 U.S.C. §1011 *et seq.*

USAA then filed an Application for Injunction Pending Appeal, setting forth the substantial economic loss and harm which would result from license revocation, even if a revocation order were stayed pending appeal. After denial by the district court, the Court of Appeals, per Judges Hunter and Garth (Mansmann dissenting) granted the injunction on November 22, 1985. (22A.)

The Third Circuit reversed the district court. Finding from the facts presented that USAA would suffer "devastating economic consequences" (Pet. App. 62a) from a license revocation order even if stayed pending appeal to a state court[3], the Court of Appeals held abstention inappropriate. The economic consequences and harm which the lower court found would be caused by abstention and license revocation were detailed at length. (Pet. App. 61a-62a.)

Because of this harm, the Court of Appeals in its *Pullman* discussion held that "the district court erred by holding that state appeal and supersedeas procedures adequately protected USAA's interests." (Pet. App. 77a.) The Third Circuit's *Younger* discussion emphasized by use of italics that *Younger* abstention would have been appropriate only if the state's appeal and supersedeas procedures "*were adequate to vindicate [USAA's] federal claims.*" (Pet. App. 75a.)

Moreover, the Third Circuit rejected the district court's holding that a countervailing state interest might

3. Petitioner's brief, acknowledging these findings, argues that "These 'findings' of potential damage by the Court of Appeals are no more than speculation, unsupported by the record." As pointed out *infra*, these findings of economic harm are not only supported by the record, but are uncontroverted.

be served by abstention. It concluded instead that Pennsylvania's interest in the regulation of the "business of insurance", properly understood under the guidelines established by this Court in *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119 (1982) and similar cases, was not implicated by the affiliation between USAA and the Bank. (Pet. App. 70a-72a.) In fact, the Court of Appeals expressed skepticism whether abstention would serve any Pennsylvania state interest whatever given the unusual facts of this case, referring to "the vague claim of risks to the state from a Texas bank not doing business in Pennsylvania." (Pet. App. 62a.)

Finally, the Third Circuit, recognizing the substantial conflict shown by USAA's Supremacy Clause claim (viz.: Congress' broad grant of plenary authority to *federal* agencies to determine who shall own, manage and operate banks within the Federal Savings and Loan System, versus Pennsylvania's insistence that USAA surrender that ownership or suffer a multimillion dollar loss of all its Pennsylvania business), held on an alternative ground that *Pullman* abstention was inappropriate here, where a strong federal preemption claim, involving no substantive constitutional interpretation, was present. (Pet. App. 63a-68a.)

The Commissioner thereafter did not seek to stay or recall the Third Circuit's mandate. Accordingly, this case was remanded to the district court. There, by order entered July 1, 1986, the district judge granted USAA a preliminary injunction against any administrative license revocation. The Commissioner did not appeal from that injunction. Instead, he announced in mid-August 1986 an intention to seek a writ of certiorari from this Court.

At the present time the only extant state proceeding (albeit enjoined) is the administrative license revocation proceeding pending before the Commissoner.

SUMMARY OF ARGUMENT

The Court of Appeals for the Third Circuit declined *Pullman* and *Younger* abstention after concluding that abstention in this case would cause the federal plaintiffs "devastating economic consequences" against which state appeal and supersedeas procedures were inadequate remedies.

The Third Circuit's *Younger* decision is not in conflict with this Court's later decision in *Ohio Civil Rights Commission et al. v. Dayton Christian Schools, Inc. et al.*, 106 S. Ct. 2718 (1986). *Dayton* emphasized that *Younger* abstention requires "an adequate opportunity" to vindicate federal claims in the state proceedings. In this case, no such adequate opportunity existed because the federal plaintiffs would suffer "devastating economic consequences" before their federal claims could be resolved.

This Court also need not review the lower court's *Pullman* decision, which squarely rested on its "findings" of the economic harm of abstention, especially in view of the presence of an alternate ground for its *Pullman* decision.

ARGUMENT

I. Unlike *Dayton Christian Schools*, The Decision Below Turned On A Factual Finding That Respondents Would Suffer "Devastating Economic Consequences" If The District Court Were To Abstain Under *Younger*.

In *Ohio Civil Rights Commission et al. v. Dayton Christian Schools, Inc. et al.*, 106 S. Ct. 2718 (1986) (hereafter "*Dayton*"), decided three weeks after the Court of Appeals' decision in this case, this Court held *Younger* abstention appropriate to allow the Ohio Civil Rights Commission to conduct an investigation into whether there was probable cause for a hearing on charges of a discriminatory discharge of a teacher.[4] The record in *Dayton* showed that the Ohio Commission had been sensitive to first amendment (i.e. religious) justifications for otherwise illegal discrimination and had sometimes dismissed complaints of religious discrimination after considering such justifications. Absent any suggestion that appellee Dayton Christian Schools would suffer great or irreparable injury from such administrative proceedings, and noting that the school's constitutional objections to any administrative remedy could certainly be presented on appeal to a state court, this Court approved a *Younger* abstention, saying: "We . . . have no reason to doubt that Dayton will receive an adequate opportunity to raise its constitutional claims." 106 S. Ct. at 2723-24.

By contrast, the precise opposite is true here. Here, the Third Circuit found that USAA would suffer "devastating economic consequences" before its federal claims could be resolved. (Pet. App. 62a.) The reason is that Pennsylvania is not here engaging in a mere investigation, as Ohio was in *Dayton*. Rather, Pennsylvania is

4. Under the administrative scheme, only after finding probable cause might a hearing be held on the charges.

here seeking the harshest of sanctions, a license revocation order, which will devastate USAA's impeccable reputation with consumers and financial institutions, frighten away policyholder renewals, suggest fraudulent activity or financial instability in the marketplace, and impair USAA's ability to represent that its policies are available nationally to the highly mobile group of armed forces officers who comprise its member-policyholders. As the Third Circuit found, a supersedeas or stay will not ameliorate these economic consequences, because of the unique nature of the proceedings at issue below.[5]

Given these unusual facts, the Court of Appeals was properly unable to find, for *Younger* purposes, that Pennsylvania's state judicial process provided USAA an "adequate opportunity" to present its federal claims in state court. Accordingly, abstention was held inappropriate.

That this is so is demonstrated by the Third Circuit's discussion of its reasons for not abstaining under *Younger*.[6] The Third Circuit took care to italicize in its opinion (Pet. App. 75a) that *Younger* abstention is appropriate only where "*the [state] proceedings are adequate to vindicate federal claims.*" By use of such emphasis, it is clear that the Court of Appeals was focusing upon the adequacy of USAA's opportunity to "vindicate" its federal claims in the state proceedings.

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5. In *Gibson v. Berryhill*, 411 U.S. 564 (1973), a case cited in *Dayton*, the economic and reputational harm there to be caused by an administrative delicensing order led this Court to dismiss the argument — similar to petitioner's here — that later state court review sufficed to provide the necessary "adequate" opportunity for resolution of the federal challenges. 411 U.S. at 577.

6. Consistent with the fact that the Commissioner's abstention motion had relied only on *Pullman* and *Burford* abstention (*Younger* abstention was added to the district court's opinion *sua sponte*), the Commissioner gave *Younger* abstention little emphasis in the lower courts.

This focus is of course utterly consistent with this Court's teaching in *Dayton* and its predecessor cases. This Court made clear in *Dayton* that *Younger* abstention may apply to administrative proceedings only if the federal plaintiff has "a full and fair opportunity" to litigate his constitutional claim. 106 S. Ct. at 2723. The crux of the Third Circuit's holding was precisely that where the particular administrative proceedings afforded the federal plaintiffs no opportunity to raise federal challenges until after they have suffered what the court had already found would be devastating economic consequences, such opportunity could hardly be deemed "adequate." Thus, such proceedings should not be treated as part of the state's judicial process for *Younger* purposes.[7]

The Commissioner begins his contrary argument by flatly saying that "The Court of Appeals reversed the District Court's holding that *Younger* abstention was proper for one reason only — USAA could not raise constitutional claims during its administrative proceeding before the Insurance Department and therefore that proceeding was not a part of the state's judicial process for *Younger* purposes." (Petition, at 27.) This argument ignores much of the Third Circuit's opinion and misconceives the true basis for the decision. What the Court of Appeals actually said was that:

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7. The inappropriateness of abstention where such abstention will cause devastating economic consequences is not only consistent with *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 140 n.3 (1970), cited by the Third Circuit, but also with *Younger*'s roots in the equitable doctrine that federal injunctions were permissible against pending state proceedings if needed to prevent great and immediate irreparable harm. Here, the devastating economic harm which USAA will suffer has been amply recognized both by the majority of the Court of Appeals panel (Pet. App. 59a-62a), and by Circuit Judges Hunter and Garth in issuing the injunction pending appeal.

> We believe a state administrative proceeding is part of its judicial process, for *Younger* purposes, *only if it provides an adequate opportunity to raise constitutional challenges.*

(Pet. App. 77a.) (Emphasis added.) In evaluating this crucial question of the adequacy of the available state procedures, the Court of Appeals, as already set forth under its *Pullman* discussion (Pet. App. 62a), had reasoned as follows:

> Weighing the legal issues and the devastating economic consequences a license revocation would impose upon USAA on the one hand and the vague claim of risks to the state from a Texas bank not doing business in Pennsylvania we conclude that the *district court erred by holding that state appeal and supersedeas procedures adequately protected USAA's interests.*

(Emphasis added.)

In short, given its finding that USAA's interests (in having a full and fair opportunity to resolve its federal claims) were not adequately protected from devastating harm by the available state appeal and supersedeas procedures, the Court of Appeals' further determination that the federal claims could not be resolved in the Insurance Department's own proceeding meant, inevitably, that abstention was inappropriate. Hence the court held that, given the facts found in this case, the state's administrative proceedings should not be considered part of the state's judicial process for *Younger* purposes.

Finally, subsequent events have made a *Younger* abstention even more inappropriate.[8] Because of the Commissioner's failure either to stay or to recall the Third

8. These developments may be considered in reviewing *Younger* abstention questions. *See, e.g., Middlesex County Ethics Committee v. Garden State Bar Association*, 457 U.S. 423 (1982).

Circuit's mandate, this case was remanded to the district court and further proceedings have been occurring. On July 1, 1986, after further briefing and oral argument, the district court issued a preliminary injunction in favor of USAA because the court found, *inter alia*, a likelihood that respondents would succeed on the merits of their preemption and other claims. The Commissioner took no appeal. The district court fixed a briefing schedule and USAA and the Commissioner have since filed supplementary briefs on the issues raised in USAA's summary judgment motion on preemption grounds. Only after such further proceedings did the Commissioner's counsel in mid-August 1986 reveal an intention to seek a writ of certiorari in this Court. But the federal action by then, with the Commissioner's full acquiescence, had "proceeded well beyond the 'embryonic stage'." Ordinarily, "considerations of economy, equity and federalism counsel against *Younger* abstention at that point." *Hawaii Housing Authority v. Midkiff*, 467 U.S. 229, 238 (1984). Given that the Commissioner himself permitted the federal machinery to proceed to and beyond the issuance of a preliminary injunction by the district court, his request that this Court now grant certiorari to permit a possible *Younger* abstention is unwarranted. If a federal injunction against further administrative proceedings had really prejudiced Pennsylvania or its Insurance Commissioner, there would have been greater effort to use the remedies available to prevent it.[9]

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9. Another reason to decline *Younger* abstention is the Third Circuit's conclusion, made in the context of its *Pullman* analysis (Pet. App. 63a-68a), that abstention is often inappropriate where the federal plaintiff presents a substantial preemption challenge. *See Capital Service, Inc. v. NLRB*, 347 U.S. 501 (1954) (abstention inappropriate where federal government has preempted field of labor policy). Here, the conflict presented is whether ownership of a federal savings and loan in Texas shall be determined by the Federal Home Loan Bank Board and the FSLIC (which, as this Court said in *Fidelity Federal Savings & Loan Association v. de la Cuesta*, 458 U.S. at 160, have "plenary authority" over such matters) or whether

II. The Court of Appeals' Alternative Reasons For Declining *Pullman* Abstention Do Not Warrant Review.

The Commissioner challenges both of the Third Circuit's alternative reasons for not abstaining under the *Pullman* doctrine. Neither challenge presents important questions and neither has merit.

A. The Third Circuit's *Pullman* Decision Rests Squarely On Its "Findings" Of The "Devastating Economic Consequences" Of Abstention.

In Part III-B of its opinion, the Court of Appeals held *Pullman* abstention inappropriate because the "devasting economic consequences" of abstention outweighed the state's countervailing interest in abstention.

In this regard, Commissioner Grode complains of what he admits were the "findings" (Petition at 43) of the Third Circuit that USAA will suffer "devastating economic consequences" from the outcome of the license revocation proceedings, even if a stay of the license revocation order were granted. *Cf. Pike v. Bruce Church, Inc.*, 397 U.S. 137, 140 & n. 3 (1970) (no abstention

NOTES (*Continued*)

such ownership shall be forcibly divested by the state of Pennsylvania (through its threatened use of delicensing power). The lower courts have consistently held that the presence of a substantial preemption challenge weighs against *Younger* abstention. *Middle South Energy, Inc. v. Arkansas Public Service Comm.*, 772 F.2d 404, 417 (8th Cir. 1985), *cert. denied*, 106 S. Ct. 884 (1986) (the legitimate state interest contemplated by *Younger* "does not exist when the state action has been preempted"); *Champion Int'l Corp. v. Brown*, 731 F.2d 1406, 1409 (9th Cir. 1984) ("Montana has no cognizable state interest in enforcing those age discrimination laws that are preempted by Federal law"); *Baggett v. Dept. of Professional Regulation*, 717 F.2d 521, 524 (11th Cir. 1983) (abstention inappropriate when "assertion of preemption went to the jurisdiction and power of the state administrative agency to proceed at all"); *Kentucky West Va. Gas Co. v. Pa. P.U.C.*, 791 F.2d 1111, 1117 (3d Cir. 1986) (*Younger*'s respect for comity is "not strained when federal court cuts off state proceedings that entrench upon the federal domain.")

where allegedly unconstitutional state regulation threatened $700,000 crop loss); *Gibson v. Berryhill, supra* (nonabstention approved where unconstitutional administrative license revocation proceeding would harm federal plaintiff). But his complaint that such findings were unsupported by the district court record is simply incorrect. To begin with, evidence of the harm of license revocation was presented to the district court by affidavit with USAA's Motion for Summary Judgment on Preemption Grounds (filed January 25, 1985). This harm was also discussed in USAA's Supplemental Brief Opposing Defendant's Abstention Motion at pp. 2-3 (filed March 1, 1985), in USAA's Memorandum Of Law In Support Of Motion For Preliminary Injunction at pp. 6-12 (filed July 11, 1985), and, after the Commissioner offered to agree to a supersedeas, was further elaborated on to the district court by the affidavit supporting USAA's Application for Injunction Pending Appeal (17A-21A) (filed October 7, 1985). Just as important, the Commissioner and his Insurance Department have never contested the devastating economic consequences of a license revocation order even if stayed, and never offered any contrary evidence.[10]

Nor can such findings be deemed "speculative", as the Commissioner suggests. Indeed, less impressive findings of harm were relied on by this Court in rejecting abstention in *Gibson v. Berryhill, supra*. In *Gibson*, state officials had sought abstention in favor of a state administrative proceeding to revoke a medical license. A three-judge district court found that, because of administrative bias, the federal plaintiffs had no meaningful opportunity to present their federal challenge to the state statute in the revocation proceeding. The state officials con-

10. Indeed, the Commissioner acknowledged on page 19 of his Brief In Opposition To Motion For Preliminary Injunction filed in the district court on September 23, 1985: "Defendant does not dispute that revocation of the license(s) of plaintiffs would create problems for plaintiffs."

tended that such an opportunity nonetheless would be provided by *de novo* review in a state court from an administrative delicensing order. This Court rejected such contention. In upholding the district court's refusal to abstain, this Court pointedly referred to the lower court's finding, similar to those in this case, that:

> [T]he revocation by the Board of appellees' licenses to practice their profession, "together with the attendant publicity which would inevitably be associated therewith, would cause irreparable damage" to the appellees for which no adequate remedy is afforded by state law.

411 U.S. at 577 n.16.[11] The Third Circuit's rejection of *Pullman* abstention here was consistent with this Court's decision in *Gibson*.[12]

B. The Court Of Appeals' Alternate *Pullman* Ground Presents No Conflict With Other Decisions.

The Commissioner finally argues against the Third Circuit's alternate holding that *Pullman*-type abstention is inappropriate in this case in light of USAA's substantial[13] preemption claim. Contrary to Commissioner

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11. This Court ultimately did decide to abstain in *Gibson* for other reasons.

12. The Commissioner also overlooks that *Pullman* abstention was also inappropriate for lack of an important countervailing state interest. The Third Circuit rightly rejected the only important state interest ever posited by the Commissioner, saying "Regulations such as Section 641 have no place in the business of insurance under McCarran-Ferguson". (Pet. App. 69a-72a.) Indeed, given that the USAA Federal Savings Bank does no business in Pennsylvania and is located in Texas, the Court of Appeals was skeptical of the existence of any Pennsylvania interest to be served by abstention, referring to petitioner's "vague claim of risks to the state from a Texas bank not doing business in Pennsylvania. . . ." (Pet. App. 62a.) This lack of an important state interest is another reason for denying *Younger* abstention in this case.

13. That USAA's preemption claim is a substantial one is underlined by the district court having granted USAA a preliminary

Grode's suggestion, this holding is not in conflict with this Court's decision to abstain in *Lake Carriers' Assoc. v. MacMullan*, 406 U.S. 498 (1972). The parties in *Lake Carriers* had agreed that federal regulations promulgated under the federal Water Quality Improvement Act would preempt the Michigan Watercraft Pollution Control Act, but only *once those federal regulations were issued and became effective* (which this Court found would be some years in the future). The justiciable controversy in that case was limited to whether the Michigan statute was constitutionally enforceable in the interim period before the federal regulations even became effective. *Id.* at 504-508. Abstention in *Lake Carriers* simply permitted Michigan to resolve its immediate state law ambiguities without risking collision with the existing federal regulatory scheme.[14]

For these reasons, this Court in *Lake Carriers* had no occasion to decide or even to discuss whether a preemption claim presents a substantial constitutional question for *Pullman* purposes. By contrast, this Supremacy Clause issue had to be considered in weighing abstention here because it was immediate and substantial: according to the Commissioner, the Pennsylvania

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NOTES (*Continued*)

injunction on July 1, 1986, reflecting that court's belief after full briefing and argument that USAA showed a substantial likelihood of success on the merits. Moreover, as this Court itself has pointed out in *Fidelity Federal*, *supra* at n.9, the Ninth Circuit has concluded that "the regulatory control of the [Federal Home Loan] Bank Board over federal savings and loan associations is so pervasive as to leave no room for state regulatory control." *Conference of Federal Savings and Loan Associations v. Stein*, 604 F.2d 1256, 1260 (9th Cir. 1979), *summarily aff'd*, 445 U.S. 921 (1980).

14. In *Lake Carriers*, however, this Court considered it settled for purposes of defining the jurisdiction of three-judge courts, that Supremacy Clause claims were not "constitutional" claims, and that such preemption claims could only be decided under the *pendent* jurisdiction of such courts if a nonfrivolous "constitutional" claim was also present. 406 U.S. at 504 n.5.

statute (Section 641) prohibited the very affiliation already approved by the federal agencies having plenary regulatory jurisdiction.

Nor does the Third Circuit's decision conflict with those of other circuit courts. In *Aluminum Co. of America v. Utilities Comm'n*, 713 F.2d 1024 (4th Cir. 1983), *cert. denied*, 465 U.S. 1052 (1984), cited by the Commissioner, the court's holding was not on *Pullman* grounds, but on *Burford* grounds. Moreover, the Fourth Circuit there merely declined to adopt Alcoa's *per se* argument that *Burford* abstention is *never* appropriate if a federal plaintiff asserts a preemption claim. Indeed, the Fourth Circuit, recognizing that a substantial preemption claim often counsels against abstention, said:

> We decline to adopt such a *per se* rule. The presence of a preemption claim, however, may in some cases require a refusal to abstain. . . . For example, abstention is inappropriate where the federal government has preempted the field . . . or where there is a direct, facial conflict between state and federal statutes. . . . In such cases, the basic premise of abstention — avoiding needless federal court intervention into important matters within the state's jurisdiction to regulate — obviously is lacking. The challenged state action clearly conflicts with preemptive federal law.

Id. at 1030 (citations omitted). In short, the Fourth Circuit's view that a substantial preemption claim is a factor which weighs against a *Pullman* abstention is consistent with the Third Circuit's opinion in this case.

The last two cases relied on by petitioner to show a conflict in the circuits are also inapposite. Neither *Druker v. Sullivan*, 458 F.2d 1272 (1st Cir. 1972) nor *City Investing Co. v. Simcox*, 633 F.2d 56 (7th Cir. 1980), addressed whether a preemption claim should be deemed a substantial constitutional question for *Pullman* purposes, because both cases turned on their own

peculiar facts. In *Druker*, the First Circuit simply allowed an abstention decision to stand because of its need for state court interpretation of unusually complex state legislation, legislation which the First Circuit variously referred to as "a riddle", and "a draftsman's corkscrew." *Id.* at 1276. And in *City Investing Co., supra*, there simply was no contention made that the federal plaintiffs' preemption claim was not a substantial constitutional claim for *Pullman* purposes.

On the other hand, as fully reviewed in Part III-C of the Third Circuit's opinion, the Ninth Circuit and Tenth Circuit Courts of Appeals have expressly addressed and discussed this issue. *Knudsen Corp. v. Nevada State Dairy Commission*, 676 F.2d 374, 377 (9th Cir. 1982); *Federal Home Loan Bank Board v. Empie*, 778 F.2d 1447, 1451 n.4 (10th Cir. 1985). These Ninth and Tenth Circuit decisions are consistent with the Third Circuit's present decision. There is no conflict among the circuits.[15]

The Commissioner also argues that this and other courts have viewed Supremacy Clause claims as "constitutional" claims. But the holdings in the cases cited by the Commissioner do not support this view. Instead, they show that Supremacy Clause claims are often considered "statutory" or "non-constitutional", depending upon the purpose such labels would serve. For example, in *Hagans v. Lavine*, 415 U.S. 528 (1974), this Court clearly recognized that preemption claims are to be considered "statutory" claims for purposes of analyzing the jurisdiction of three-judge courts. Indeed, in that case

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15. The Commissioner also complains that the Third Circuit's *Pullman* decision would allow "any plaintiff" to "defeat an otherwise appropriate abstention simply by appending a Supremacy Clause claim." This argument lacks merit. Such argument would have been correct only if the Third Circuit had adopted a *per se* rule that *Pullman* abstention is *never* appropriate if any preemption claim is present.

this Court pointed out, in language since used for guidance by lower courts in abstention cases that, "where the Supremacy Clause is implicated: 'the federal courts are particularly appropriate bodies for the application of preemption principles.' " 415 U.S. at 550. And consistent with *Swift & Co. v. Wickham*, 382 U.S. 111 (1965), relied on by the court below, a preemption claim in another case cited by the Commissioner (*International Brotherhood of Electrical Workers v. Public Service Commission*, 614 F.2d 206 (9th Cir. 1980)) was held to be a nonconstitutional statutory claim. *Id.* at 211.

In summary, this case, like *Pike v. Bruce Church, Inc.*, *supra*, and *Gibson v. Berryhill*, *supra*, but unlike *Dayton*, presents findings that devastating and irreparable harm will be suffered before the federal plaintiff has an opportunity to have his federal claims resolved in the state court system. This Court decided in *Gibson* that, when such unique facts are present, the administrative proceeding (with its right of appeal) may well not afford the delicensed federal plaintiff an adequate opportunity to litigate its federal or constitutional challenges. The Third Circuit's decision, which preceded *Dayton*, fully accords with this principle using the particular findings here present. No purpose would be served by review of these findings in this Court or by remand of this case.

CONCLUSION

For these reasons, the petition for a writ of certiorari should be denied, in all respects.

Respectfully submitted,

Michael L. Browne
Christopher K. Walters*
J. Thomas Morris
Reed Smith Shaw & McClay
1600 Avenue of the Arts Bldg.
Broad and Chestnut Streets
Philadelphia, PA 19107

Robert B. Hoffman
Reed Smith Shaw & McClay
300 North Second Street
Harrisburg, PA 17108

Counsel for Respondents

*Counsel of Record
December 3, 1986

APPENDIX

FEDERAL HOME LOAN BANK BOARD

No. 83-708
Date: December 15, 1983

WHEREAS, the Federal Home Loan Bank Board has considered the record and merits of the application of Robert F. McDermott, et al., San Antonio, Texas, dated April 4, 1983, for permission to organize a new Federal stock savings bank to be known as "USAA Federal Savings Bank" to be located at, or in the immediate vicinity of, Huebner Road and Interstate 10, San Antonio, Texas; and

WHEREAS, it is determined that the applicants are persons of good character and responsibility, that there is a necessity for such an association in the area to be served, that there is a reasonable probability of its usefulness and success, and that it can be established without undue injury to properly conducted existing thrift and home-financing institutions; and

WHEREAS, the Board has, as required by the Community Reinvestment Act of 1977, taken into account the applicant's proposed statement to meet the credit needs of the entire community it will serve, including the low- and moderate-income neighborhoods therein;

WHEREAS, in a related filing the United States Automobile Association has applied to acquire 100% of the shares to be issued by the USAA Federal Savings Bank; and whereas any approval of said holding company application would be subject to the condition that USAA and any subsidiary thereof agree not to engage in investment banking activities and to restrict activities related to securities brokerage and advising mutual funds to less than 5% of USAA's assets on a consolidated basis;

THEREFORE, IT IS HEREBY RESOLVED, that said application is hereby approved provided that the following conditions are complied with in a manner satisfactory to the Supervisory Agent at the Federal Home Loan Bank of Dallas not later than six months from the date of this

Resolution, unless, prior to the expiration of such period, a request to the said Supervisory Agent for an extension of such time limit shall have been received and granted; provided further that, except as herein required, there have been no substantial changes in the information currently before the Board relating to said applicant; and provided further, that there has been received no additional information having an adverse bearing on any feature of the application, and that the applicant has:

1. Submitted, to the Supervisory Agent, one signed and three conformed copies of such proposed charter and bylaw along with a certification by the secretary of the association that the charter conforms to Section 552.3 of the Federal Regulations and the bylaws contain sufficient provisions to govern the association in accordance with the requirements of Section 552.6 through 552.6-4 of the Federal Regulations and shall not contain any provision which is inconsistent with applicable laws, rules, regulations, or the charter, and has submitted such documentation to the said Supervisory Agent for approval;

2. Amended, if necessary, all security forms to conform with the Rules and Regulations for Insurance of Accounts and has obtained approval from the Supervisory Agent for the issuance of the security forms;

3. Submitted a written opinion of its counsel that the securities adopted by the association can be legally issued under applicable law and regulations and its charter and bylaws;

4. Not opened for business prior to compliance with all rules and regulations of Federal and State law;

5. Submitted, in a form satisfactory to the Supervisory Agent at the Federal Home Loan Bank of Dallas, a comprehensive business plan covering a period of three years. The Supervisory Agent shall monitor the applicant's progress in implementing the business plan for a period of three years;

6. Upon issuance of a Federal charter, submitted evidence that all funds collected on subscriptions are adequately safeguarded and that all Rules and Regulations of the Federal Savings and Loan System and other applicable Federal laws and regulations have been complied with;

7. Obtained blanket bond coverage from an approved surety company, in at least the amount required by the Insurance Regulations;

8. Obtained approval from the office of General Counsel at the Federal Home Loan Bank Board of the offering circular prior to the issuance of any stock in the Federal Savings Bank, or if an exception is claimed, a copy of the legal opinion regarding the proposed offering and any information required for non-public offerings;

Installed, or arranged to install, a modern system of accounting and supporting records, including standards substantially equivalent to those contained in the Standard Accounting Manual and an adequate system of internal checks and controls;

10. Established permanent nonwithdrawable capital and paid-in surplus aggregating at least $3,000,000, which amount is to be divided between permanent stock and paid-in surplus in a manner satisfactory to the Corporation;

11. Submitted a certification to the Supervisory Agent of the adoption by the stockholders of the institutions's proposed stock option plan;

12. Received the approval of the Principal Supervisory Agent, pursuant to Section 563.41 of the Insurance Regulations, of any real property transactions between the association and USAA for its office quarters;

13. Executed and submitted an agreement with the Corporation which shall provide that, in consideration of the granting of insurance of its accounts, the operating policies as hereinafter set forth as requirements for insurance shall be effective as of the date of insurance of its accounts and shall remain in full force and effect as long as its accounts are insured by the Corporation, unless, with the written approval of the Corporation, a change therein is made, said agreement to include provisions, satisfactory to the Corporation:

(a) The composition of the institution's management shall comply with the provisions of: (1) the Depository Institutions Management Interlocks Act of 1978, as amended, (2) the regulations implementing that Act, (3) Section 563.33 of the Rules and Regulations for Insurance of Accounts ("Insurance Regulations"), (4) the Change in Savings and Loan Control Act and the Savings and Loan Holding Company Act (both of which require prior notice and approval for acquisitions and changes of control of FSLIC insured stock institutions) and (5) any future statutory or regulatory changes related to the composition of the institution's management;

(b) The institution shall adopt a home financing policy which is consistent with economical home financing and the purposes of Title IV of the National Housing Act;

(c) Lending plans and policies, covering lending territory, and origination of loans will be equally extended to all sources of origin; interest rates, premiums, service charges and other loan costs will be such as to enable the institution to obtain and hold the best loans available;

(d) The institution shall establish and maintain, at the proposed or other acceptable location, independent office quarters, accessible to the general public consistent with general industry practice, at which the association shall conduct its business, including the taking of deposits;

(e) The institution shall establish a construction loan procedure which includes the use and recording of adequate inspection reports on all properties securing such loans;

(f) The institution shall adopt loan appraisal practices and procedures conforming to the best established practices in the industry;

(g) The institution shall establish a procedure, with respect to hazard insurance coverage on all properties mortgaged to the institution, allowing mortgage borrowers a free choice in the selection of hazard insurance brokers or agents;

(h) Adequate internal checks and controls shall be established and maintained;

(i) A plan shall be adopted to ensure the continuation or succession of competent management in the event of the managing officer's incapacity or resignation;

(j) No dividend, other than a stock dividend on permanent nonwithdrawable capital, shall be paid if the net worth of the institution, as defined

in the Insurance Regulations, is or would become, as a result of the payment of such dividend, less than that required by Section 563.13 of the Insurance Regulations, as said section currently reads or may hereafter be amended;

(k) Any amount remaining in the paid-in surplus account after the absorption of any deficit shall remain as part of the permanent capital structure of the institution;

(l) Except with the Principal Supervisory Agent's prior approval, brokered deposits, including rollovers therefrom, shall be limited to five percent of the institution's deposit base for the period between the commencement of operations and the beginning of the first full fiscal year and for three years following the beginning of the first full fiscal year;

(m) A plan shall be adopted to ensure diversification of investments and avoidance of concentration in a particular type of investment and in a particular geographic location;

(n) The institution shall adopt a business plan, as described in Section 571.6(b) of the Insurance Regulations, which shall include provisions for the prior approval by the Principal Supervisory Agent of any material change in, or deviation from, the business plan during the period beginning with the commencement of operations and the beginning of the first full fiscal year and for the three years following the beginning of the first full fiscal year; and

(o) That the institution shall provide for employment of a qualified full-time executive managing officer, subject to approval by the Principal Supervisory Agent, on a salaried basis

who shall be charged with full administrative and managerial responsibilities of the institution under policies established by its board of directors. In the event of the managing officer's removal, incapacity or resignation during the period between the commencement of operations and the beginning of the first full fiscal year and for the three years following the beginning of the first full fiscal year, the continuation or succession of competent management will also be subject to the Principal Supervisory Agent's approval.

By the Federal Home Loan Bank Board

J. G. Finn
Secretary

December 28, 1983

George H. Ensley, President
USAA Financial Services Company
USAA Building
San Antonio, Texas 78288

Application by USAA Financial Services Company (FINCO), San Antonio, Texas (H-506), a subsidiary of the USAA group of companies, San Antonio, Texas, for permission to acquire control of USAA Federal Savings Bank (USAA Bank), San Antonio, Texas

Dear Mr. Ensley:

The subject application has been reviewed by this office in keeping with the provisions of Section 408(e) of the National Housing Act, as amended, and Section 584.4 of the Regulations for Savings and Loan Holding Companies.

Pursuant to the authority delegated to this office, the application is hereby approved, provided that the following conditions are complied with in a manner satisfactory to this office:

1. The proposed acquisition shall be consummated no later than 120 days after the date of this letter;

2. FINCO shall file an affidavit with the Supervisory Agent certifying to the consummation of the acquisition in accordance with the provisions of the

subject application and specifying the exact number of shares of stock of the insured institution acquired;

3. FINCO shall stipulate to the Bank Board that as long as it controls the subject institution, it will cause the net worth of USAA Bank to be maintained at a level consistent with that required by Section 563.13(a)(2)(ii)(a) of the Rules and Regulations for Insurance of Accounts for de novo institutions, and where necessary to infuse sufficient additional equity capital, in a form satisfactory to the Supervisory Agent, to effect compliance with such requirement;

4. FINCO shall stipulate to the Bank Board that, unless prior written approval has been obtained from the Supervisory Agent with the concurrence of the Director of the Office of Examinations and Supervision, dividends paid by USAA Bank in any fiscal year shall be limited to 50 percent of net income for that fiscal year, as reflected on its quarterly financial reports to the Bank Board, provided that any dividends permitted under this limitation may be deferred and paid in a subsequent year, but in no event may dividends be paid that would reduce the subject institution's net worth below the level required by the Insurance Regulations;

5. The USAA group of companies agree not to engage in investment banking activities and, specifically (1) agree not to underwrite corporate debt and equity securities; and (2) agree not to act as principal in the sale of corporate debt and equity securities.

6. USAA Investment Management Company and any other affiliate of the USAA group of companies that should become engaged in managing,

advising or servicing open end investment companies or become engaged in securities brokerage activities at some future date, agree that their aggregate assets will not exceed 5 percent of the assets of USAA on a consolidated basis.

7. The USAA group of companies may request relief from compliance with conditions 5 and 6, which will be granted if future legislative, judicial or regulatory action occurs which, in the Board's view, eliminates the need for imposition of the conditions.

Very truly yours,

Joseph E. Settle
Supervisory Agent

JES:TH:jo

BEFORE THE INSURANCE COMMISSIONER
OF THE
COMMONWEALTH OF PENNSYLVANIA

IN RE:	: ALLEGED VIOLATIONS:
	:
UNITED SERVICES AUTOMOBILE	: Section 641 of the Insurance
ASSOCIATION	: Department Act of 1921, Act of
USAA CASUALTY COMPANY	: May 17, 1921, P.L. 789, *as*
USAA LIFE INSURANCE	: *amended*, 40 P.S. §281.
COMPANY	:
USAA ANNUITY AND LIFE	:
INSURANCE COMPANY	:
USAA Building	:
San Antonio, TX 78288	: Docket No. C84-12-5

ORDER TO SHOW CAUSE

And Now, this 24th day of December, 1984, pursuant to the statutes captioned above and in accordance with 1 Pa. Code §35.14, Respondents are hereby ORDERED to appear at a formal administrative hearing before the Insurance Commissioner of the Commonwealth of Pennsylvania, or his duly designated Presiding Officer, and TO SHOW CAUSE why the Insurance Commissioner, upon consideration of the Factual Allegations pursuant to Applicable Law, and in accordance with Procedures cited herein, should not impose the specified Penalties, as said terms are described below.

It Is Hereby Ordered that Respondents file an Answer to this Order to Show Cause in writing within the time specified herein, in accordance with 1 Pa. Code §35.37. Such Answer shall specifically admit or deny each of the Factual Allegations made herein, and shall set forth the facts and state concisely the matters of law upon which Respondents rely. If Respondents fail to file an Answer within the time allowed herein, the Factual Allegations shall be deemed admitted, and the Insurance Commissioner may issue an Order imposing such Penalties as he deems appropriate.

FACTUAL ALLEGATIONS

1. Respondent United Services Automobile Association ("USAA") is a Texas-domiciled reciprocal insurance exchange with its principal place of business at USAA Building, San Antonio, Texas.

2. USAA is licensed in this Commonwealth to engage in the businesses of fire and allied insurance, inland marine and physical damage insurance, ocean marine insurance, general liability insurance, burglary and theft insurance, automobile liability insurance and personal property insurance pursuant to Subsections (b) (1), (2) and (3) and (c) (4), (6), (11) and (13) of Section 202 of the Insurance Company Law of 1921, Act of May 17, 1921, P.L. 687, *as amended*, 40 P.S. §382.

3. Respondent USAA Casualty Insurance Company is a Texas-domiciled stock insurance company with its principal place of business at USAA Building, San Antonio, Texas.

4. USAA Casualty Insurance Company is licensed in this Commonwealth to engage in the businesses of fire and allied insurance, inland marine and physical damage insurance, ocean marine insurance, general liability insurance, burglary and theft insurance, automobile liability insurance and personal property insurance pursuant to Subsections (b) (1), (2) and (3) and (c) (4), (6), (11) and (13) of Section 202 of the Insurance Company Law of 1921, Act of May 17, 1921, P.L. 687, *as amended*, 40 P.S. §382.

5. Respondent USAA Life Insurance Company is a Texas-domiciled stock insurance company with its principal place of business at USAA Building, San Antonio, Texas.

6. USAA Life Insurance Company is licensed in this Commonwealth to engage in the businesses of life insurance and annuities and accident and health insurance pursuant to Subsections (a) (1) and (2) of Section 202 of the Insurance Company Law of 1921, *supra*, 40 P.S. §382.

7. Respondent USAA Annuity and Life Insurance Company is a Texas-domiciled stock insurance company with its principal place of business at San Antonio, Texas.

8. USAA Annuity and Life Insurance Company is licensed in this Commonwealth to engage in the business of life insurance and annuities pursuant to Subsection (a) (1) of Section 202 of the Insurance Company Law of 1921, *supra*, 40 P.S. §382.

9. USAA Casualty Insurance Company, USAA Life Insurance Company and USAA Annuity and Life Insurance Company are wholly-owned subsidiaries of USAA.

10. USAA Financial Services Company (formerly known as USAA Development Company) is a wholly-owned subsidiary of USAA acting as the holding company for USAA's non-insurance subsidiaries.

11. On or about April 14, 1983, USAA Financial Services Company (then known as USAA Development Company), filed an application with the Federal Home Loan Bank Board for a *de novo* Federal Savings Bank Charter for the USAA Federal Savings Bank.

12. Concurrent with the aforementioned filing, USAA Financial Services Company (then known as USAA Development Company), filed with the Federal Savings and Loan Insurance Corporation an Application H(e) (1) to serve as a unitary savings and loan holding company.

13. The aforementioned applications were approved effective December 15, 1983, and the USAA Federal Savings Bank began operations on December 30, 1983.

14. As such, USAA, through its subsidiary, USAA Financial Services Company, currently owns and controls the USAA Federal Savings Bank.

15. As such, USAA constitutes a savings and loan holding company as defined by Section 641(a) of the Insurance Department Act of 1921, Act of May 17, 1921, P.L. 789, *as amended*, 40 P.S. §281(a).

16. As such, USAA Casualty Insurance Company, USAA Life Insurance Company and USAA Annuity and Life Insurance Company are subsidiaries of a savings and loan holding company as defined by Section 641(a) of the Insurance Department Act of 1921, *supra*, 40 P.S. §641(a).

APPLICABLE LAW

Based on the foregoing Factual Allegations, it is alleged that Respondents have violated the following statute: Section 641(b) of the Insurance Department Act of 1921, Act of May 17, 1921, P.L. 789, *as amended*, 40 P.S. §281(b), which states in its entirety:

> No lending institution, public utility, bank holding company, savings and loan holding company or any subsidiary or affiliate of the foregoing, or officer or employee thereof, may, directly or indirectly, be licensed or admitted as an insurer or be licensed to sell insurance in this State either as a broker or as an agent except that a lending institution or bank holding company, subsidiary or affiliate of a lending institution may be licensed to sell credit life, health and accident insurance and to sell and underwrite title insurance in accordance with regulations promulgated by the Insurance Commissioner.

Reference should also be made to the following statutes and regulations:

1. Administrative Agency Law, 2 Pa.C.S. §§101-508 and §§701-704.

2. General Rules of Administrative Practice and Procedure, 1 Pa. Code §§31.1-35.193, 35.225-35.251.

3. Special Rules of Administrative Practice and Procedure, 31 Pa. Code §§56.1-56.3.

PENALTIES

After the Procedures set forth herein, if the Insurance Commissioner finds the Factual Allegations set forth herein to be true and correct, and determines that Respondents have violated any provision of Applicable Law, the Insurance Commissioner at his discretion may impose the following Penalty: Revocation of any and all insurance licenses issued by the Commissioner and currently held by Respondents.

PROCEDURES

The formal administrative hearing in this matter shall be held in accordance with the Administrative Agency Law, Act of April 28, 1978, P.L. 202 (2 Pa.C.S. §§101-508 and 701-704); General Rules of Administrative Practice and Procedure, 1 Pa. Code §§31.1-35.193, 35.225-35.251; Special Rules of Administrative Practice and Procedure, 31 Pa. Code §§56.1-56.3; and other relevant procedural provisions of law.

The hearing shall be held before the Insurance Commissioner of the Commonwealth of Pennsylvania, or his duly designated Presiding Officer, in accordance with 1 Pa. Code §35.185.

Respondents may appear, with or without counsel, and offer testimony or other evidence in their behalf.

In the event Respondents fail to respond to this Order to Show Cause or to appear at said hearing, the Factual Allegations contained herein shall be deemed admitted, and the Insurance Commissioner shall issue an Order imposing such Penalties cited herein as he, in his discretion, deems appropriate.

ORDER RETURNABLE at such time and place as shall be fixed for the convening of the formal administrative hearing on this Order to Show Cause. Answers, motions preliminary to those at hearing, protests, petitions to intervene, or notices of intervention, if any, must be filed in writing with the Docket Clerk, Insurance Department, Room 1342 Strawberry Square, Harristown State Office Building No. 1, Harrisburg, Pennsylvania 17120 no later than twenty (20) days from the date notice of this Order is published in the *Pennsylvania Bulletin*.

NOTICE of this Order to Show Cause shall be given by the Insurance Department by forwarding a copy by first-class mail to the Respondents named herein and by publication in accordance with 1 Pa. Code §35.105 and 31 Pa. Code §57.1.

/s/

JOHN J. SHEEHY
Chief Deputy Insurance Commissioner

UNITED STATES DISTRICT COURT
FOR THE MIDDLE DISTRICT OF PENNSYLVANIA

UNITED SERVICES AUTOMOBILE ASSOCIATION, et al.	:	
	:	CIVIL ACTION NO. 84-1596
Plaintiffs,	:	
v.	:	
WILLIAM J. MUIR, III	:	
Defendant.	:	
STATE OF TEXAS	:	
	:	SS
COUNTY OF BEXAR	:	

AFFIDAVIT OF WILLIAM McCRAE IN SUPPORT OF APPLICATION FOR INJUNCTION PENDING APPEAL

William McCrae, being duly sworn, upon his oath deposes and says:

1. I am both Senior Vice President and Secretary of the United Services Automobile Association ("USAA") and am authorized to make this Affidavit on its behalf.

2. USAA has grown to become one of the largest, most successful and most reputable insurance companies in the United States. Its excellent reputation is evidenced by the September, 1984 issue of "Consumer Reports" which rates USAA as second highest in the country among automobile insurance companies with regard to claimants' overall satisfaction with the handling and settlement of claims. Additionally, the August, 1985 issue of "Consumer Reports" rates USAA as second highest in the country among homeowners' insurance companies with regard to claimants' overall satisfaction. Copies of the "Consumer Reports" articles are attached hereto as Exhibit "A."

3. USAA has consistently received the highest possible rating (i.e. "A+") with regard to financial position and operating performance by the A. M. Best Company ratings. A copy of the most current A. M. Best Company rating is attached hereto as Exhibit "B."

4. USAA's success is due in part to the low claims ratio history of the class of persons it services, namely, commissioned officers in the United States armed services as well as candidates for commissions.

5. USAA and co-plaintiffs are licensed to sell insurance in all fifty states. USAA's availability in all fifty states is an important factor for the highly mobile officers in the armed forces which are serviced by the USAA group of companies.

6. By letters dated July 3, 1984 and August 27, 1984, and in subsequent meetings, the Pennsylvania Insurance Department expressed the view that USAA's ownership of the USAA Federal Savings Bank in San Antonio, Texas, constitutes a violation of Section 641 of the Insurance Department Act of 1921 as amended (40 P.S. §281) (hereafter "Section 641"). Copies of these letters are attached hereto as Exhibits "C" and "D" respectively.

7. Moreover, prior to the filing of this lawsuit, the Defendant's Insurance Department advised representatives of USAA that USAA must divest the Bank or else the Insurance Department would initiate proceedings to revoke the licenses of USAA to transact business in Pennsylvania.

8. Defendant Muir, during his tenure as Acting Insurance Commissioner, has entered an order requiring one or more other insurance companies to relinquish their Pennsylvania insurance licenses by

reason of their affiliation with an out of state banking institution. A copy of such order is attached as Exhibit "E."

9. On December 24, 1984, Defendant's Insurance Department issued an administrative "Show Cause Order" alleging that USAA and co-plaintiffs are in violation of Section 641 by reason of their affiliation with the Bank. A copy of the Insurance Department's Show Cause Order is attached hereto as Exhibit "F."

10. Before filing the administrative Show Cause Order, Defendant Muir advised enforcement personnel of the Insurance Department that "A plain reading of §641 with the broad prohibition would be adopted." *See* Exhibit "G" attached hereto.

11. Administrative hearings to revoke plaintiff's insurance licenses have been rescheduled for November 14, 1985. A pre-hearing conference is scheduling for October 15, 1985. *See* Exhibit "H" attached hereto.

12. An order revoking plaintiffs' insurance licenses is substantially certain to occur following the administrative hearings in defendant's Insurance Department in view of:

(a) The past enforcement of Section 641 by the Department;

(b) The representations of the Department that USAA must divest the Bank or suffer revocation of its licenses;

(c) The service of an Administrative Show Cause Order alleging that USAA and co-plaintiffs are in violation of Section 641;

(d) The statement of the Defendant that a "plain reading of Section 641 with its broad prohibition" would be adopted;

(e) The fact of USAA's affiliation with the USAA Federal Savings Bank is admitted.

13. The Defendant's Insurance Department has never expressed any view contrary to its position that USAA and co-plaintiffs are in violation of Section 641.

14. An order revoking the licenses of USAA and co-plaintiffs will have a devastating and irreparable impact upon the business of USAA and co-plaintiffs, which will *not* be mitigated by the availability of supersedeas procedures in the state court system.

15. An order revoking plaintiffs' licenses, and the inevitable resulting publicity, will cause confusion and uncertainty in the minds of the nearly 40,000 policyholders in Pennsylvania who have chosen to insure their lives, homes, automobiles and other property with plaintiffs. Many policyholders will not understand the reason for the license revocation or the effect on them pending appeal.

16. An uncertain number of these nearly 40,000 policyholders will likely terminate their relationship with USAA and co-plaintiffs upon learning that the Pennsylvania Insurance Department has revoked plaintiffs' licenses. This will occur even with supersedeas due to the uncertain status of plaintiffs' licenses pending appeal.

17. An uncertain number of prospective policyholders will be dissuaded from insuring their lives, homes, automobiles and other property due to the uncertain status of plaintiffs' licenses pending appeal. USAA's competitors will be able to make use of

information concerning the status of these licenses in their marketing efforts.

18. It appears that USAA and co-plaintiffs will be required to notify the Insurance Departments in other states concerning any such order of revocation, despite a supersedeas. Most of these states do not have statutes similar to Section 641. Plaintiffs will be subject to damage to its outstanding reputation as well as unnecessarily increased regulatory scrutiny in these states.

19. License revocation is an extreme sanction, usually applied, if at all, only in cases where an insurance company has engaged in grossly illegal or fraudulent practices or where the company is in poor financial condition. Even with supersedeas, USAA and co-plaintiffs will suffer serious damage to their goodwill and excellent reputation in Pennsylvania and elsewhere if the licenses of these companies are revoked.

20. Only intervention by this court can prevent irreparable harm to USAA and co-plaintiffs as described above, and ensure that plaintiffs receive a fair adjudication of their constitutional rights *before* suffering such harm by reason of an order revoking plaintiffs' licenses.

/s/ WILLIAM MCCRAE

William McCrae

Sworn and subscribed
before me this 14th day
of October, 1985

/s/ LORETTA C. LANICEK

Notary Public Loretta C. Lanicek

My Commission expires 11/30/88

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

#C-64

November 8, 1985

No. 85-5662

UNITED SERVICES AUTOMOBILE ASSOC., et al.

vs.

MUIR, WILLIAM J., III, etc.

Appellants

(M.D. Civil 84-1596)

Present: HUNTER, GARTH, and MANSMANN, *Circuit Judges*.

1. Appellant's motion for injunction pending appeal, or in the alternative, for expedited argument, in which it requests that this Court enter an order enjoining appellee, pending appeal, from revoking appellant's Pennsylvania insurance licenses by reason of their federally-approved affiliation with the USAA Federal Savings Bank in San Antonio, Texas, in the above-entitled case.

Respectfully,

/s/
Deputy Clerk 7-5019

enc.
ad

The foregoing Motion for injunction pending appeal is granted. Motion to expedite is denied.

Judge Mansmann would deny the motion for injunction pending appeal.

By the Court,

/s/ JAMES HUNTER, III
Judge

Dated: November 22, 1985
ad/cc: Christopher K. Walters, Esq.
Ellis M. Saull, Esq.

IN THE UNITED STATES DISTRICT COURT
FOR THE MIDDLE DISTRICT OF PENNSYLVANIA

UNITED SERVICES AUTOMOBILE ASSOCIATION, ET AL.,	:	
Plaintiffs	:	
v.	:	CIVIL NO. 84-1596
WILLIAM J. MUIR, III,	:	
Defendant	:	

ORDER

And Now, this 1st day of July, 1986, upon consideration of Plaintiffs' Renewed Motion For Preliminary Injunction and Brief in support thereof, and finding that unless this order is entered irreparable injury will result to Plaintiffs before final adjudication of this matter, it is ORDERED and DECREED as follows:

Defendant William J. Muir, III, his successors in office, and his and their officers, agents, servants, employees and attorneys and those in active concert or participation with them are enjoined and restrained, pending final judgment in this case, from taking any further actions in connection with the administrative enforcement proceedings pending in the Pennsylvania Insurance Department against plaintiffs herein. This Preliminary Injunction shall take effect upon the posting by plaintiffs of security pursuant to F.R.C.P. 65(c) in the amount of $10,000.00.

By the Court:

R. DIXON HERMAN
United States District Judge